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HAPPY NEW YEAR

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EXPERT EXPLAINS ABCs OF U.S. RULES OF ORIGIN AND MARKING

By Ivan Koves
From December 2004 Issue of IOMA's Report on Managing Exports and Imports

Accurately determining the country of origin of imported or exported goods is one of the most important—and challenging —tasks facing international trade pros. Rules of origin, which determine the national identity of a product, are crucial to determining admissibility, import duties owed, possible applicability of quotas, anti-dumping duties and countervailing duties (ADD/CVD), and marking requirements. Mistakes in using rules of origin under Free Trade Agreements can expose exporters and their overseas customers to real problems. Finally, U.S. trade statistics are deepen- dent on accurate country of origin determinations as reported by exporters and importers.

At a recent Webcast sponsored by trade software provider and consultant Vastera, expert Ivan Koves led participants through the fundamentals of the complex U.S. rules of origin and marking requirements. (For upcoming Vastera Webcasts and seminars on export/import topics, see www.vastera.com.)

U.S. Rules of Origin Background

"Non-preferential rules of origin are intended to apply to every imported item on a neutral, consistent basis," Koves explains. "The second way rules of origin are applied," he adds, "is preferentially." This is usually associated with a trade agreement such as NAFTA, or a national policy like the Generalized System of Preferences (GSP)."

"A problem for trade pros is that rules of origin are often not consistent from country to country," Koves points out. While the World Trade Organization (WTO) has been attempting for several years to harmonize rules of origin to achieve transparency and consistency, that goal still lies well in the future. "In addition, marking requirements— how you mark a good for entry into a nation—are usually not consistent among countries," Koves explains. "How goods must be marked for entry into the United States differs significantly from how they must be marked for entry into China, for example."

"It's pretty obvious where something comes from, so what can be so hard about deciding country of origin?" Koves asks. He then illustrates how complex the process can be by describing a not untypical product of today's global sourcing and distribution marketplace. Koves gives the example of a sailing yacht with a high-tech hull and keel designed and built in Australia; a mast, boom, and rigging manufactured in the United States; sails cut and sewn in France; and deck and interior fixtures added in London. "The sailboat is sealed, painted, and launched in England," Koves adds. "If Spain has a quota allowing only 150 boats to be imported from Australia and 400 from the United States, but no quotas for France or England, which quota system applies—if any?" He adds that if tariff rates differ for each country, which one is applicable?

"That's not even considering trade sanctions such as anti-dumping and countervailing duties, which are unique to each country" he continues. "And say the government procurement rules of the U.S. Navy limit boat purchases to ones built in the United States, would this boat qualify?" U.S. Rules of Origin—Non-Preferential "Thankfully, U.S. non-preferential rules of origin are similar to those of most other developed countries," Koves says. "Non-preferential rules," he explains, "apply to the world in general and establish the nationality of products for policy measures such as:

Admissibility (whether the item can enter or not). "If the product is from Iran, Libya, or Cuba, for example, you won't be able to import that item into the United States—with rare exceptions."

Duty: "In the U.S. tariff schedule there are different duty rates for Column 1 (normal trade relations with duty rates typically under 2% on average) and Column 2 (abnormal trade relations with rates pegged at 35%)."

Quotas, e.g., textile imports—Customs Regulations (19 CFR 12.130, 102.21).

Anti-dumping orders: "The United States has a lot of anti-dumping legislation," Koves explains, "and rules of origin play a big role in making such determinations." These orders are specific to manufacturers/sellers but have an 'all others' category as well.

Marking: "This is a huge issue in the United States, especially for those selling at retail," Koves says. Products from Canada and Mexico have their tariff-shift based rules established in 19 CFR 102. All other countries come under the "substantial transformation" rules (19 CFR 1334).

U.S. trade statistics: Non-preferential rules of origin come in two basic “flavors,” Koves notes:

1) ‘Wholly obtained’: This rule is for goods that are wholly the growth, product, or manufacture of one country. “In today’s manufacturing environment,” says Koves, “‘wholly obtained’ rules generally apply to agricultural goods, mined resources, and fish products caught offshore.” Because manufacturing inputs now come from so many countries it’s rare to find manufactured goods that are ‘wholly obtained.’

2) ‘Substantial transformation’: This is the rule most often used and applies to imported goods made from materials from more than one country. “The rule of substantial transformation itself falls into two categories,” Koves adds.

a) A case-by-case decision to determine the one country in which the item was “substantially transformed” into an article with a name, character, or use distinct from that of its components. “This is a case-by-case and sometimes subjective decision,” Koves explains.

b) A tariff shift-based rule, applicable to items imported from Canada or Mexico, based on the Harmonized Tariff Schedule (HTS) and similar to NAFTA preferential rules. “You look at HTS classification for all the components of the item and determine whether the specific change laid out in the regulations occurred,” says Koves. “That determines the country in which some or all of the components classified under various tariff classifications were changed into an article with a tariff classification called for by the rule.”

U.S. Rules of Origin—Preferential

Preferential rules of origin are specific to such trade agreements as the U.S.-Chile and U.S.-Singapore FTAs, Andean Trade Preference Act, Automotive Products Trade Act, NAFTA, GSP, and Caribbean Basin Initiative. The two most typically dealt with are the GSP and NAFTA. As Koves explains, “GSP provides for duty free entry of most classes of merchandise from a designated beneficiary developing country, as set out in the United States HTS, if:

“the article is imported directly from such a country into U.S. customs territory and if the sum of

“1) the cost or value of materials produced in that country plus
“2) the direct costs of processing operations performed in that country equal at least 35% of the appraised value of the article.

“Such complex calculations for GSP-eligible goods often trip up importers,” notes Koves. “Customs can and will ask to see calculations by which the 35% figure is reached.” NAFTA is the classic example of preferential rules of origin. The origin rule for goods that are not “wholly obtained” is based on 1) a strict tariff shift method and 2) the regional value content (RVC) method.

U.S. Marking Requirements

“U.S. marking rules apply to nearly all items of foreign origin,” says Koves. “While U.S. origin articles need not be marked, invoices and entry summaries must declare the origin of all imported items.” “The marking law is essentially political,” he adds. Its purpose is to inform U.S. consumers of the origin of the merchandise they are buying. In an exception to the substantial transformation rule, the Federal Trade Commission has ruled “Made in the USA” can only be a marking if the goods are made from 100% U.S. materials using 100% U.S. labor. “Key exceptions to the U.S. marking requirements,” says Koves, “are as follows:

good is from a NAFTA partner, will be used in manufacture, is sold at retail, or is distributed as a gift,” Koves explains.

There are serious sanctions for failure to comply with marking requirements:

“Articles not properly marked at the time of importation are subject to additional duties unless properly marked, exported, or destroyed under CBP supervision prior to liquidation of the entry (typically 10% of value),” Koves says.

“Removing, destroying, altering, covering with the intent of concealing the country of origin marking on an imported article is a criminal offense,” he cautions.

Basic U.S. Marking Rules

● Size: marking must be large enough to be read by person with “normal vision.”

● Location: where visible to casual handling and won’t be covered by additions.

● Durability: not removable except by deliberate effort. Stencils and stamps best; hanging tags if durable enough to reach ultimate purchaser; adhesive labels emergency only).

● Abbreviations (e.g., for countries): frowned on by Customs & Border Protection.

● “Made in” or “Product of”: only precedes country name if another country name also appears on article or container.

● Containers: don’t require own marking, but unusual containers, imported empty or full, must be marked: “Container made in (country).”

● Combined articles: an article to be combined with another in U.S. but not so as to be “substantially transformed” must be marked: (name of imported article) made in (country).”

UNDERSTANDING INCOTERMS

Incoterms are standard trade definitions most commonly used in international sales contracts. These terms are devised and published by the International Chamber of Commerce.

Among the best-known Incoterms are EXW (Ex works), FOB (Free on Board), CIF (Cost, Insurance and Freight), DDU (Delivered Duty Unpaid), and CPT (Carriage Paid To).

ICC introduced the first version of Incoterms - short for "International Commercial Terms" - in 1936. Since then, ICC expert lawyers and trade practitioners have updated them six times to keep pace with the development of international trade.

Most contracts made after 1 January 2000 will refer to the latest edition of Incoterms, which came into force on that date. The correct reference is to "Incoterms 2000". Unless the parties decide otherwise, earlier versions of Incoterms - like Incoterms 1990 - are still binding if incorporated in contracts that are unfulfilled and date from before 1 January 2000.

Versions of Incoterms preceding the 2000 edition may still be incorporated into future contracts if the parties so agree. However, this is course is not recommended because the latest version is designed to bring Incoterms into line with the latest developments in commercial practice.

The English text is the original and official version of Incoterms 2000, which have been endorsed by the United Nations Commission on International Trade Law (UNCITRAL). Authorized translations into 31 languages are available from ICC national committees.

Correct use of Incoterms goes a long way to providing the legal certainty upon which mutual confidence between business partners must be based. To be sure of using them correctly, trade practitioners need to consult the full ICC texts, and to beware of the many unauthorized summaries and approximate versions that abound on the web.

ICC now publishes a brief introduction to Incoterms on a new special section of its website. The section does not provide all the answers but will help understanding of what Incoterms are for and how they are organized. It describes how to order Incoterms in the original English version and many of the world's main languages from ICC Publishing in Paris and New York, or ICC national committees around the world.

The site includes for the first time the Preambles to each term, in read-only format. The Preambles explain the areas the terms cover but do not spell out the obligations of buyer and seller - information that can be obtained only by consulting the full published texts of the 13 Incoterms.

For more information on Incoterms go to http://www.iccwbo.org/index_incoterms.asp

U.S.–AUSTRALIA FREE TRADE AGREEMENT

The Free Trade Agreement between the United States and Australia is scheduled to take effect on January 1, 2005. Australia's GDP, growing at an annual rate of around 4.5 percent, is larger than any country in the region except Japan or China. It has a well-established commercial and business infrastructure, which contributes to a stable economic environment. Unemployment, inflation and interest rates are at close to historically low levels. Australia continues to be an excellent prospect for both U.S. exports and investment.

For more information on doing business with Australia contact us at little.rock.office.box@mail.doc.gov
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U.S.-MOROCCO FREE TRADE AGREEMENT

The U.S.-Morocco Free Trade Agreement, which is scheduled to take effect on January 1, 2005, will provide fair conditions of competition for trade between the two countries, improve the business environment, facilitate and increase U.S. exports in a number of sectors such as telecommunications, tourism, energy, environment, insurance and finance. (Over the past 6 years, U.S. exports to Morocco averaged $475 million annually). Removal of Moroccan tariffs will be phased-in slowly for a few very sensitive products and sectors, specifically textile and beef, poultry and wheat markets.

The U.S.-Morocco FTA's investment rules will make Morocco quite attractive to U.S. companies searching for opportunities in the Mediterranean, Middle East, or Africa. Investment provisions, new market access, and enhanced IPR protection will make Morocco the ideal platform for other foreign investors to produce products for export to the United States and Europe, as well as to the Maghreb and West Africa.

For more information on doing business with Morocco contact us at little.rock.office.box@mail.doc.gov
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NEW TRADE PACTS WITH LAOS AND ARMENIA

President Bush recently signed into law a broad trade package that extends normal trade relations to Laos and Armenia, suspends tariffs on hundreds of products not produced domestically, and repeals a dumping law ruled illegal by the World Trade Organization. The entire article appears on the U.S. State Department website at:
http://usinfo.state.gov/eur/Archive/2004/Dec/07-732694.html.

FREE AND SECURE TRADE (FAST) PROGRAM

Canada and the United States (U.S.) have agreed to align, to the maximum extent possible, their customs commercial programs along their shared border. This agreement marks the creation of the Free and Secure Trade (FAST) program, which is the result of a shared objective to enhance the security and safety of Canadians and Americans, while enhancing the economic prosperity of both countries.

Canada and the U.S. are working together to end threats to public security and safety, while keeping their shared border open to the free flow of low-risk, legitimate trade by:

- adopting a common approach to risk management; and
- partnering with those in the trade community who have a history of compliance and are committed to the integrity of their supply chain management processes, using compatible and advanced technology.

The FAST program will feature:

Greater integrity in supply chain management processes by offering expedited clearance processes to those carriers and importers who have been approved for Canada's Customs Self Assessment (CSA) and Partners in Protection (PIP) programs and have enrolled in the U.S. Customs and Border Protection's Customs Trade Partnership Against Terrorism (C-TPAT) program. The PIP and C-TPAT are similar programs that call for clients' use of business processes that minimize exposure to criminal elements by securing the supply chain.

Streamlined and, where appropriate, integrated registration processes for drivers, carriers, and importers, minimizing administrative requirements while ensuring that only low-risk trade chain participants with sound and secure business practices are extended the privileges of the FAST program.

Expedited clearance of low-risk trans-border shipments by reducing the information required to meet customs requirements, dedicating lanes at major crossings to FAST participants, using common technology, and focusing limited physical examinations to matters related to public security and safety.

Integrated and advanced technology such as transponders used by both Canada and the U.S., facilitating the clearance of low-risk shipments, and relieving the clients' participation costs.

Dedicated compliance account managers who will build and maintain client partnerships and monitor clients' compliance with program requirements.
For more information on the FAST program, visit: www.cbsa.gc.ca/fast.

For more information on the Customs Self Assessment (CSA) Program, visit:
www.cbsa.gc.ca/import/csa/menu-e.html

COMMERCIAL AGENTS IN THE EUROPEAN UNION

U.S. companies interested in entering or expanding business in the European Union may find the use of commercial agents an attractive way to access the market. However, companies should be aware of EU regulations and policies that may affect relationships between principals and their commercial agents. This report reviews the provisions outlined by "Council Directive 86/653/EEC on the coordination of the laws of the Member States relating to self-employed commercial agents," and how its application by the European Union Member States has implications for U.S. businesses in the European Union. Contact us at little.rock.office.box@mail.doc.gov, Fax 501-324-7380, or phone 501-324-5794 for a copy of this 7-page report.

COMMERCIAL ENCRYPTION EXPORT CONTROLS EFFECTIVE DECEMBER 9, 2004

Effective December 9, 2004, the Export Administration Regulations (EAR) have been amended in order to streamline and strengthen export and re-export controls on encryption items. Further information on this policy can be found at:
http://a257.g.akamaitech.net/7/257/2422/06jun20041800/edocket.access.gpo.gov/2004/04-26992.htm

JANUARY 12, 2005 DEADLINE FOR ADVERTISING IN MARCH/APRILISSUE OF COMMERCIAL NEWS USA

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FEBRUARY EXPORT SEMINARS

- Export Operations – Feb. 14-15 – Memphis
- Export Controls – February 16- Memphis
- NAFTA Workshop – February 17 – Memphis

For details go to http://www.unzco.com

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